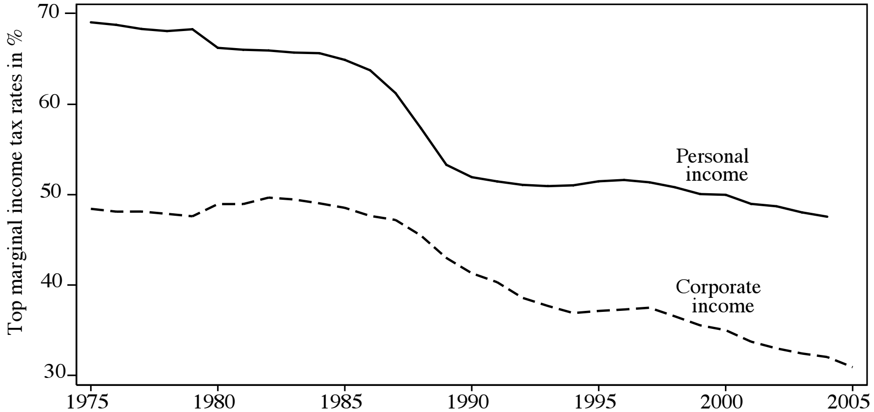
chapter one | introduction

In the last 30 years, income tax rates for corporations and persons declined substantially in advanced OECD countries (Figure 1.1). Between 1975 and 2005 the headline tax rate on corporate income of advanced OECD countries fell on average from around 50 to around 30 per cent, the top rate on personal income from almost 70 to well below 50 per cent.[1] The decline in corporate tax rates started in the mid-1980s—after the famous US tax reform of 1986—and shows no signs of abating. The downward movement in top personal rates began in the mid-1970s but became more pronounced for a few years after the US reform.

These downward trends in tax rates have figured prominently in the literature on the domestic effects of economic internationalisation (e.g. Genschel 2005). However, many social scientists have been sceptical as to the causal role of tax competition, partly because the cuts in statutory tax *rates* have not generally led to a fall of income tax *revenues* (OECD 2004c). These authors have instead highlighted the importance of changing ideas, partisan politics and democratic institutions at the domestic level (e.g. Garrett 1998a; Hallerberg and Basinger 1998;

Figure 1.1: Top marginal income tax rates in OECD countries, 1975–2005



Notes: Unweighted averages. Sources: See appendix

Ottaviani 2002; Swank and Steinmo 2002; Steinmo 2003; Campbell 2004).

The evidence on the effects of domestic factors, though, is far from conclusive. For instance, Wagschal (2001: 154) reports that with respect to recent tax reforms the partisan composition of governments has no explanatory power; and the findings of Hallerberg and Basinger (1998; 1999) seem to contradict conventional wisdom about partisan ideology. For one thing, they claim that in response to the US tax reform of 1986 left-leaning governments in other countries made *deeper* cuts in corporate tax rates than their right-leaning counterparts. For another, they claim that the existence of powerful veto players reduced the magnitude of corporate and personal tax cuts, which, combined with the first result, may suggest that *right-leaning* veto players blocked tax cuts. While ad hoc explanations for such findings abound—e.g. that left-wing governments have to pay a 'risk premium' to international investors in the form of lower corporate tax rates (Hallerberg and Basinger 1998: 345)—there is no *coherent* theoretical account that can explain both the downward trend in tax rates and the international variation in income tax structures.

This study seeks to contribute to such an account. Its analytical focus is rather specific. As to the dependent variables, it mainly focuses on the statutory features of tax systems, such as top marginal rates on different types of incomes. This focus has two related rationales. First, for reasons that will become clearer in the development of the argument, I am strongly interested in the basic structure of income taxation, e.g. whether capital and labour income are taxed jointly or separately; statutory tax rates are a crucial part of this structure. Second, I shall argue that one main 'function' of the income tax has been to bring an element of progressivity into the tax system at large. Marginal rates are important in this respect because they are reasonable, albeit rough, indicators of progressivity. The two arguments are related: for while effective progressivity also depends on the breadth of the tax base (tax credits, deductions, allowances etc.), I shall argue that this breadth does itself follow to a large extent from the basic structure adopted. Many loopholes in capital income taxation were (and still are) the result of policymakers' efforts to tax labour and capital income under a *joint* tax schedule. Once this effort is abandoned, loopholes can be closed without requiring large cuts in the marginal tax rates *on labour*. In sum, then, statutory tax rates are useful indicators if we distinguish systematically between different types of incomes.

As to the independent variables, my focus is on the interaction of party ideology, veto institutions and socio-economic constraints (i.e. economic, administrative and political constraints). Such a focus is hardly an innovation. In practice, however, political science analyses often take insufficient account of economic constraints. The main reason, I contend, lies in the ambiguity of the term 'policy preference' (cf. Ganghof 2003). Actor-centred approaches such as veto player theory (Tsebelis 2002) rightly focus on how the interaction of actors' policy preferences (which are taken to be temporarily fixed) and legislative rules produces legislative outputs. Yet policy preferences are not ends in themselves. Rather, they are means for achieving certain policy *outcomes*. It would be more accurate therefore to speak of policy *strategies*. These strategies derive from parties' ideologies as well as from more specific beliefs about the mapping of policies on to outcomes, given constraints and trade-offs. The problem with policy preferences is that they change (in line with changing beliefs about the mapping of policies on to outcomes) and, partly as a result, are difficult to measure. Empirical studies often ignore this problem by assuming that indicators of 'party positions' based on expert surveys or party manifestos can be regarded as proxies for policy preferences. This can be misleading, though, because such party positions are often at best proxies of outcome preferences. If this is true, we have to include socio-economic constraints explicitly in our theoretical and empirical models in order to avoid misleading inferences. To explain when, how and to what extent party ideology shapes legislative outcomes, we have to understand how domestic and international constraints shape parties' *policy strategies* and how legislative institutions shape their *legislative strategies*.

THE MAIN ARGUMENTS

I argue that the common sense view of partisan income tax policy is basically correct, even if applied to the tax reforms of the 1980s and 1990s: leftist (rightist) parties continue to prefer higher (lower) income taxes, more (less) progressive taxation, and higher (lower) taxes on the capital income of well-off taxpayers. Yet to understand the interaction of party ideology and veto institutions we have to develop a more accurate understanding of socio-economic constraints in income taxation. At the most general level, I argue that these constraints are more severe than has been acknowledged in the political science literature. Hence my account is intended to both qualify and specify argument about ideational changes and policy learning. More specifically, my explanation can be summarised in terms of four core arguments. First, tax competition has been a crucial contributing cause of cuts in statutory corporate tax rates (the tax competition argument). Second, tax competition has had an indirect pull-down effect on tax rates on higher personal incomes (the spill-over argument). Third, this pull-down effect has been counteracted by domestic pressures to maintain a certain degree of progressivity in the income tax system (the domestic constraints argument). Fourth, the importance of party ideology and veto institutions is conditional upon the tightness of structural constraints: in corporate taxation, where international constraints are tight, it is low; in personal taxation (of wages), where domestic constraints are less tight, it is greater. I shall elaborate on the four arguments in turn.

The tax competition and spill-over arguments

The first argument is that tax competition was an important contributing cause of cuts in statutory corporate tax rates, despite the fact that corporate tax bases were broadened and corporate tax revenues did not generally fall. The theoretical reason is that there are various mechanisms through which tax competition puts pressure on *statutory* tax rates. One of these mechanisms is the profit-shifting behaviour of multinational firms, which is to a large extent driven by statutory rates. Another has to do with competition for *profitable* investment. Roughly speaking, the more profitable an investment project, the more important is the statutory corporate tax compared to tax allowances. As a result of these types of mechanisms, policymakers had a strong incentive to cut statutory corporate tax rates even if this had to be paid for by reducing tax allowances.

The most important type of evidence supporting this argument is the *correlation between tax rates and country size*. The economic theory of tax competition predicts that if two countries of unequal size compete with each other for mobile tax bases, the smaller country will in equilibrium have a lower tax rate. In a small country with a small existing capital stock, a tax cut does not lead to large revenue losses. At the same time, relatively high revenue can be expected due to the inflow of foreign capital. Hence, if tax competition has played a role in the setting of corporate tax rates, we would expect an increasingly positive association between corporate tax rates and country size. I shall show that this is exactly what we see. There has in fact been a strong convergence of corporate tax rates in advanced OECD countries, but it has been *conditional* convergence (Sala-i-Martin 1996; Ganghof 2005c).

But does tax competition also limit the *outcomes* national policymakers can achieve in corporate taxation? Or can policymakers still achieve the same outcomes as before, only with a different mix of policies? I believe tax competition constrains corporate tax outcomes in at least one sense. It has long been argued in political science and economics that a system that taxed very profitable investment significantly higher than less profitable investment *increases* tax efficiency and mitigates the trade-off between economic efficiency and redistribution (e.g. Przeworski and Wallerstein 1988; Frank 1999, 2000; Layard 2005). To the extent that this view is true, tax competition tends to make the structure of corporate taxation *less* efficient, at least with respect to the investment incentives of domestic and less profitable firms. For if reforms have to be revenue-neutral, effective tax reductions for profitable foreign direct investment have to be paid for by higher taxes on less profitable and domestic firms. Hence tax competition on statutory corporate tax rate is a serious constraint, especially for parties—typically left parties—that would prefer taxing enterprises with fairly high marginal tax rates but an investment-friendly tax base.

Note that this argument is *not* challenged by explanations that highlight domestic policy learning and the international diffusion of neo-liberal ideas (e.g. Garrett 1998b; Swank 1998; Swank and Steinmo 2002). These explanations rightly highlight the fact that policymakers cut tax rates and broadened tax bases in order to 'level the playing field' and make capital income taxation more 'market-conforming'. As I shall explain in more detail in Chapter three, however, this argument refers to a different analytical dimension of income tax policy. The question how equally policymakers want to treat different types of taxable income or different types of economic activities is logically independent of the question of how 'investment-friendly' a tax base they want to have. In other words, cutting statutory corporate tax rates was by no means a necessary condition of a level playing field. There was, in principle, a choice to make about the level of 'investment-friendliness' at which the playing field was to be levelled—and this choice was constrained by tax competition.

There is a second reason why corporate tax competition tends to constrain tax policy outcomes, which is related to the second main argument of this book. Corporate taxes function as a *safeguard* for the personal income tax, and this function is generally best fulfilled if the corporate tax rate is equal to the top personal tax rate. If it is much below the top personal rate, high-income taxpayers have large incentives to use the corporate legal form in order to shield some of their income from progressive taxation. A large 'tax rate gap' (between corporate and personal taxation) thus reduces the administrative efficiency of income taxation at large and provides policymakers with incentives to reduce marginal income tax rates for high-income taxpayers. Hence, tax competition on statutory corporate tax rates makes it more costly for policymakers to maintain high marginal income tax rates on high personal incomes and tends to lead to a flattening of income tax schedules. In fact, I will show that this spill-over effect has at least *contributed* to the downward trend in top personal income tax rates after the US tax reform in the mid-1980s. This is the spill-over argument.

The domestic constraints argument

The third argument qualifies the second: if there were no domestic goals other than 'market-conformity' and administrative efficiency, one could expect policymakers in all countries to reduce the personal rate to the level of the top corporate rate (Stotsky 1995: 282; Tanzi and Zee 2000: 130). Figure 1.1 shows that this has not happened. Between 1975 and 1989 the average gap between the two top rates was almost cut in half, from around 20 to around 10 percentage points. As I will show in the case studies that follow, this reduction was no coincidence but reflected policymakers' deliberate attempts to close the tax rate gap; Germany, Australia and New Zealand actually managed to close it completely in 1977, 1988 and 1989, respectively. After 1989, however, when more and more countries implemented their responses to the US reform of 1986, the average tax rate gap widened again (to more than 15 per cent in 2004), with corporate tax rates being cut more heavily than top personal rates. The reason, I contend, is that there are domestic constraints in personal income taxation that are absent in corporate taxation.

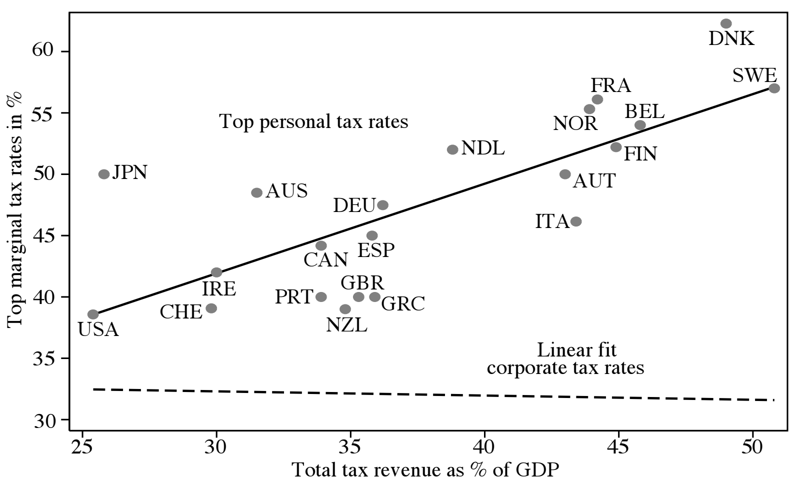
The most important constraint is the given level of total taxation in a country. Much of the total tax burden falls on wages—in the form of income taxes, social security contributions and indirect consumption taxes—and one function of the income tax has traditionally been to introduce an element of progressivity into wage taxation at large. For this reason, the higher the total tax burden, the more difficult it becomes for policymakers to reduce marginal tax rates on high incomes. This is the *domestic constraints* argument.

This summary of the argument is of course simplified. The constraint implied by large total tax burdens plays out in two different ways depending on the how much of the overall tax burden on wages takes the form of direct taxes on income. This point is best explained by way of examples:

- In a country such as *Denmark*, where a high total tax burden (around 49 per cent of Gross Domestic Product (GDP) goes together with a very high income tax burden (almost 30 per cent of GDP), it seems impossible to lower the top personal tax rate of more than 60 per cent down to the corporate rate, currently 30 per cent, without significant reductions in progressivity and revenue (*cf.* Ganghof 2005b).
- In a country such as *Austria*—where a high total tax burden (around 43 per cent of GDP) goes together with a rather moderate income tax burden (roughly 13 per cent of GDP)—bringing down the top personal rate of 50 per cent to the corporate rate of 25 per cent would be rather easy, but only because a large part of labour 'taxation' takes the form of social security contributions and general consumption taxes. Since this additional labour taxation is proportional and in part regressive, the progressive income tax tends to assume a 'progressivity adjustment' function within the overall system of wage taxation.

Figure 1.2 visualises the argument. It shows, for the year 2004, the correlations between total tax burdens on the one hand and top marginal tax rates on corporations and persons on the other. For corporate tax rates the figure only shows the regression line. This line is almost identical to a flat line at the average level of corporate tax rates (32 per cent) because there is no systematic relationship between total tax burdens and corporate tax rates. In contrast, top personal income taxes do tend to increase with total tax burdens. High-tax countries such as Denmark and Sweden also tend to have relatively high top personal rates, where-

Figure 1.2: Top marginal tax rates and total tax levels in OECD countries, 2004



Notes and sources: See appendix

as low-tax countries such as Ireland or the USA also tend to have relatively low top personal rates.

Figure 1.2 also helps us to connect the three arguments discussed so far. We have seen that in a perfect 'market-conforming' income tax, the corporate tax rate would be equal to the top personal rate. In the absence of tax competition, governments would have been able to achieve this equality by letting the corporate rate follow the top personal rate. In Figure 1.2, the 'corporate' regression line would then be roughly equal to the 'personal' line. Yet due to tax competition, corporate tax rates had to fall (the tax competition argument), which had two effects. On the one hand, many countries also cut their top personal rate (more than they would have done otherwise) in order to keep the tax rate gap moderate. Hence corporate tax competition has contributed to a downward shift of the 'personal' regression line (the spill-over argument). On the other hand, high tax burdens on wages constrained policymakers' willingness and ability to cut top personal income tax rates, so that the tax rate gap also increased again after the late 1980s, especially in high-tax countries. As a result, the regression line for top personal tax rates in Figure 1.2 has a pronounced upward slope (the domestic constraint argument).

One follow-up question raised by Figure 1.2 is this: if the combination of tax competition and domestic constraints led to a sizeable tax rate gap in most advanced OECD countries, what happened to the goal of 'market-conforming' income taxation emphasised in the political science literature? I shall explore this question and point out a 'trilemma' for policymakers. The traditional normative ideal on which most OECD countries' income tax systems had officially been built was that of 'comprehensive' or 'uniform' income taxation (e.g. Goode 1976). An ideal uniform income tax puts all annual income—both capital income and wages—of a taxpayer into a basket and subjects it jointly to a common, often progressive, tax rate schedule. 'Market-conformity' had been a crucial element of this ideal. For if all types of income are taxed jointly and hence subjected to the same marginal tax rates, the playing field is levelled. In addition, joint taxation of all income was also seen as a precondition for taxation according to taxpayers' 'ability to pay', because all types of income contributed equally to this ability. Now, the problem was that the ideal was nowhere put in practice and that the income taxes actually implemented were in many ways pathological. This fact, together with competitive pressure on corporate tax rates, forced policymakers to make a clearer choice between three stylised options:

- *Flat income tax*: This option was a comprehensive income tax with radically reduced marginal tax rates. The rationale of this option is that very low marginal tax rates enable policymakers to clean up the income tax base and to align the top personal tax rate with a *competitive* corporate tax rate. Its Achilles heel is reduced progressivity and/or revenue-raising potential in the taxation of wages.
- *Differentiated income tax*: The logic of this option is to maintain a comprehensive income tax system with higher marginal tax rates, but allow lower rates on capital income wherever the costs of taxation would otherwise become too

large, e.g. in the taxation of corporate profits retained in the company. The Achilles heel of this model is that these kinds of 'targeted' tax rate cuts for very sensitive capital income render capital income taxation less market-conforming and more arbitrage-prone.

- *Dual income tax*: This option abandons the ideal of comprehensive income taxation (as it is usually understood) and *separates* the income taxation of labour and capital. Whereas wages are taxed progressively, all types of capital income are subject to a uniform proportional tax rate. The Achilles heel of this model is that it implies a very systematic and visible tax discrimination of wages as well as complicated rules for splitting the income of small businesses into its capital and labour components.

As this list shows, maximising the goal of 'market-conforming' capital income taxation is costly. It involves either a reduction in the progressivity and/or revenue-raising potential of the income tax (the flat tax option) or an administratively costly and *prima facie* inequitable separation of labour and capital taxation within the income tax (the dual income tax option). Not surprisingly, therefore, no advanced OECD country has implemented a truly market-conforming income tax system.

The conditional importance of politics argument

In 2004, two of the countries with the smallest gap between the top tax rates on corporate and personal incomes were the USA and New Zealand. The USA comes closest to an equality of the two rates if we take average tax rates at the state level into account; the marginal tax rates on corporate and personal income both stood at around 40 per cent in 2004. This is not surprising from the perspective adopted here, because the US economy is both large and characterised by a relatively low tax burden. The case of New Zealand is more puzzling. Although New Zealand is very small, the tax rate gap was only 6 percentage points in 2004 (39 per cent minus 33 per cent); and all through the 1990s New Zealand actually maintained a strict equality of the two at a level of 33 per cent. Between 1989 and 1999 New Zealand would have been a clear outlier in Figure 1.2. One main reason for this is the fact that New Zealand was governed by a one-party 'Labour' majority government that was dominated by 'neo-liberal' politicians and faced no veto point in addition to the parliamentary majority.[2] This leads us to discuss the final main argument of this study.

This argument is one about the conditional importance of party ideology and veto institutions. It has been argued that party ideology and veto institutions were important in shaping income tax rates (Hallerberg and Basinger 1998; Wagschal 1999a; Tsebelis 2002: 203–4). But these arguments suffer from a lack of analytical differentiation. First, they do not distinguish sufficiently between outcome and policy preferences. If socio-economic constraints are very strong, differences in party ideology are unlikely to translate into differences in policy preferences. And if policy preferences do converge, the partisan composition of government and the number of veto points or players are unlikely to affect policy outputs systematically.

The second lack of analytical differentiation follows from the first: existing hypotheses about veto players and tax rates have not been formulated as being conditional upon the ‘tightness’ of socio-economic constraints. Based on the arguments presented above, such a formulation becomes possible. As to the setting of corporate tax rates, theory and evidence suggest that competitive pressures are quite significant, so that the partisan composition of government cannot be expected to be very important. I shall present qualitative and quantitative evidence supporting this expectation—and thus indirectly also the tax competition argument.

In contrast, the setting of top personal income tax rates (on labour) income is less constrained. The reason is that, whereas governments cannot unilaterally increase their size or reduce the intensity of corporate tax competition, they can unilaterally choose to reduce the level of taxation and the degree of wage tax progressivity. As a result, party ideology and veto institutions can be expected to be more important. The case of New Zealand provides an example for this importance. I shall provide qualitative and quantitative evidence that this example can be generalised. Right-leaning parties tend to use their power in government or parliament to reduce and flatten income taxes, while left-leaning parties tend to defend progressivity and revenue-raising capacity of personal income taxes (on labour incomes).

METHODOLOGICAL APPROACH AND CASE SELECTION

While there is much conceptual and theoretical debate in the social sciences about methodology, I believe that most inferences, in the social sciences and elsewhere, can usefully be described by a very general ‘model’ of inductive inference called *Inference to the Best Explanation* (Bird 1998; Lipton 2004). We are interested in a certain phenomenon P and think of possible explanations of P. If putative explanation E is the best available explanation of P, we infer that E is the actual explanation of P. To make a list of putative explanations, we rely heavily on existing background knowledge, and to determine the ‘best’ of these potential explanations we rely on certain desiderata. For example, good explanations should supply *mechanisms* that can account for correlations between different kinds of events. Good explanations should also have *power* in the sense that they can explain several distinct and disparate facts and are able to integrate or combine with other explanations. A third good-making feature is *simplicity*.

Some further remarks about important desiderata seem useful at this point. One important desideratum is the integration of one explanation with others. I believe that the more recent political science literature on taxation suffers from a lack of integration with previous findings as well as with well-established knowledge in economics. For instance, in their seminal work on the political economy of taxation, Przeworski and Wallerstein (1988) argued that systems with fairly high rates but an investment-friendly tax base mitigate the trade-off between efficiency and redistribution and should therefore be attractive for policymakers, especially those on the left (see also Garrett and Lange 1991). More recently, it was emphasised that low tax rates and broad bases are efficient and that base-broadening allowed high-tax countries to defend their revenue levels despite tax rate cuts (Garrett 1998b; Swank 1998; Swank and Steinmo 2002). But this 'revisionist' argument is itself in need of explaining: if the old Przeworski-Wallerstein argument is now believed to be wrong, we need an explanation of why this is the case. If it is believed to still hold, we need an explanation of why countries *nevertheless* cut tax rates and broadened the tax base (Wallerstein and Przeworski 1995). In the analysis that follows, I try to answer these kinds of questions.

This goal of integrating new explanations with existing ones should not be confused with a search for *complete* explanations. As noted above, my analytical focus is rather specific. For example, I have no systematic interest in the role of interest groups in the politics of income taxation. Part of the reason why incompleteness is less of a problem than often thought has to do with the 'pragmatic' aspects of explanation (Scriven 1966; Van Fraasen 1980; Garfinkel 1981; Hausman 2001; Tucker 2004). That is, explanations are first and foremost answers to Why-questions, and the kind of explanation one develops therefore greatly depends on the precise structure of the questions one asks. Different choices of explanatory variables follow to a large extent from different choices of questions and hence different explanatory *interests*. For instance, if one asks why two countries that are very similar with respect to socio-economic constraints and partisan-institutional configurations have implemented very different tax reforms, interest groups may be an important part of the answer. However, my interest is in Why-questions for which party ideology, legislative power and socio-economic constraints may provide important parts of the answers. Different choices of explanatory variables simply amount to different ways of carving up the social world into possible alternatives, and the goal of this book is merely to show that a focus on the interaction of party ideology, legislative power, and socio-economic constraints can help to answer a number of Why-questions that do or ought to figure prominently in the political science literature.

Another important desideratum of 'Inference to the Best Explanation' is that explanations explain *diverse* evidence and that they explain *in detail*. It follows that historical, case-specific evidence and more precise quantitative evidence should, if possible, be combined. Most of the evidence used in this book is qualitative. One reason is that much of the analysis is more descriptive and exploratory than confirmatory. Because there is not much in the political science literature on the politics of income tax *structure*, I want to understand in some detail how policymakers perceived the relevant trade-offs, e.g. the trade-offs associated with the choice between dual and differentiated income taxation. Developing this understanding requires detailed case analysis.

Another reason for relying strongly on case studies is that the interaction of party ideology, veto institutions and socio-economic constraints is often too complex to be modelled in regression analyses with a very small number of cases. For the same reason, the regression evidence I do provide as a complement to the qualitative analysis is based on rather simple models. In the helpful terminology of Clarke (forthcoming), I try to follow the 'logic of research design' rather than the 'logic of control'. That is, rather than adding—in the (often dubious) hope of reducing omitted variable bias—ever more variables and interaction terms to the regression equation, I try to build simple models that are focused on *discriminating between competing explanations* (see also Achen, forthcoming). I acknowledge the fact that regression results are first and foremost certain kinds of multivariate *observations*. As such they don't provide explanations but can help in discriminating between them (Hoover 1994, 2002; see also Freedman 1991; Berk 2004).

This perspective also implies that the quality of measurement is of the utmost importance. As Atkinson (2004: 178) rightly notes (and demonstrates with an example from the political science literature), it is often wrongly suggested by quantitative scholars that 'data quality is of footnote importance, and that empirical findings are robust to the choice of data'. In fact, many existing regression analyses of top marginal income tax rates are based on inconsistent data sets, containing *general government* tax rates for some countries and *central government* tax rates for others. I have assembled a tax rate data set that consistently measures general government tax rates, taking into account the often complex ways in which tax rates and tax bases at different government levels are linked (see appendix).

The qualitative evidence is based on case studies of tax reforms in seven countries: Australia, Denmark, Finland, Germany, New Zealand, Norway and Sweden. The time period under consideration is the period from the mid-1980s to the early 2000s. My original research extended until 2001 but for this publication I have updated the qualitative and quantitative evidence as much as possible. The seven countries were selected to maximise similarity in some respects and dissimilarity in others, and to allow some degree of 'nesting' individual case studies in case comparisons as well as narrow case comparisons in broader ones.

The seven countries are dissimilar with respect to their *levels of total taxation* (Figure 1.2).[3] As argued above, these levels constitute part of the domestic economic constraints policymakers face. Hence, by letting these levels vary between countries, the risk of 'selection bias' is reduced (King *et al.* 1994). Second, while all seven countries are parliamentary systems with fairly disciplined parties, they are very dissimilar with respect to the *relevant constellations of veto players and other influential actors*. As I will explain in more detail in Chapter two, the seven countries cover many of the partisan-institutional configurations that can exist in parliamentary democracies.

As to similarities, there are two sub-groups of countries the members of which adopted very similar approaches to income taxation, either before the US tax reform of 1986 or afterwards. One group is the four Nordic countries, which all tried to implement the model of dual income taxation. The other group is the Oceanic countries and Germany which, before the US reform, were the only countries that had implemented a very ambitious form of uniform income taxation by aligning the corporate tax rate with the top rate on personal incomes.

Of course, while the two Oceanic countries, like the Nordic countries, are also geographically close to one another and similar on many important background variables, Germany differs from Australia and New Zealand in many important aspects. In addition, the German case is unique in various ways, e.g. due to the presence of a powerful constitutional court as an additional veto player. For this reason, the case study on Germany will be somewhat more detailed than those on the other countries. The German case study is nested in a comparison with Australia and New Zealand, and this three-country comparison is part of the broader seven-country comparison.

THE STRUCTURE OF THE BOOK

Chapter two discusses a number of conceptual and methodological problems in the comparative analysis of legislative politics and outlines the approach adopted in this study. A central aspect of this approach is the *inference to* (rather than 'measurement' of) partisan policy preferences based on an in-depth analysis of the trade-offs and constraints parties face. The next two chapters provide this analysis: Chapter three focuses on the explanation of intertemporal policy change, Chapter four on the explanation of international policy differences. Chapters five through seven contain the seven case studies. Chapter eight summarises the case evidence and complements it with quantitative evidence on the interaction of party ideology, socio-economic constraints and veto institutions. Chapter nine draws conclusions on the tax policy options available to OECD countries both at the national and international level.

NOTES

1 Unless otherwise noted, all averages reported in this book are unweighted and refer to 21 advanced OECD (Organisation for Economic Cooperation and Development) countries. See the appendix for the set of countries, country abbreviations used as well as variable definitions and data sources.

2 The third country with a tax rate gap of 6 percentage points or lower in 2004 is Greece, another country characterised by one-party majority governments and the absence of strong legislative veto points. In addition to the case study on New Zealand in Chapter five, I shall discuss the cases of the United States and Greece in more detail in Chapter eight.

3 Of course, taxation levels *before* the mid-1980s are more important for the purpose of case selection, but these were very similar to those shown in Figure 1.1.